



Supreme Court of the United States

OCTOBER TERM, 1943.

No.

DANIEL S. GILLMOR, HENRY H. ABRAMS and PYRAMID
COMMERCIAL CORPORATION, suing on its own behalf and
on behalf of all other owners and holders of First
Consolidated Mortgage 5% Gold Bonds, etc.,
Petitioners,

—against—

THE INDIANAPOLIS GAS COMPANY and CITY OF INDIANAPOLIS.

BRIEF IN SUPPORT OF PETITION.

Opinions Below.

No opinion was rendered by the United States District Court for the Southern District of Indiana.

The opinion of Circuit Court of Appeals for the Seventh Circuit (per Circuit Court Judge Kerner) has not yet been officially reported. It appears in its original form at page 413, and in its amended form at page 478, of the record.

Jurisdiction.

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925, c. 229. The judgments of the Circuit

Court of Appeals sought to be reviewed herein were entered on June 10, 1943. A timely petition for rehearing was denied by the Circuit Court of Appeals on August 2, 1943.

Statement of Fact.

The statement of facts and questions presented are set forth in the petition.

Argument.

POINT I.

The decision of the Circuit Court herein is in conflict with the decision of the Circuit Court for the Eastern District of Virginia.

The Circuit Court has ruled that the mortgage involved herein provides "that whatever action might be taken to secure payment of the bonds and coupons should be subject to the control of the holders of a majority" of the bonds.

The mortgage itself, however, contains no language which expressly, or by necessary implication, confers such broad authority of control upon the majority bondholders.

The only provisions in the mortgage for majority control are set forth in Article VII. This article consists of two paragraphs which deal with the mortgage security. Under the first paragraph, the majority bondholders are authorized to control the action of the trustees for the enforcement of the lien of the security. Under the second paragraph, connected with the first in its subject matter and by the conjunctive "and", the majority bondholders are

authorized, in the event of any proceeding by the trustees with respect to the mortgage security, to agree upon a binding plan or scheme of reorganization.

Upon the basis of the grant of these clearly limited powers of control to the majority bondholders, the Circuit Court has concluded that the mortgage herein provides for the right of the majority to control the minority bondholders by any action, including a plan which involves neither the mortgage security nor the action of the trustee and which does not constitute a plan of reorganization.

This broad construction of the provisions of the mortgage with respect to majority control over the minority, and the consequent holding that the non-assenting bondholders are bound by the extra-judicial plan accepted by the majority, is in direct conflict with the ruling of the Circuit Court for the Eastern District of Virginia in *Manning v. Norfolk & Southern R. R. Co.*, 29 Fed. 838.

In the *Manning* case the mortgage expressly provided that a majority of the bondholders could instruct the trustee to waive a default in interest. Pursuant to such instruction by the majority bondholders, the trustee did waive a default in interest for five years. The Circuit Court for the Eastern District of Virginia, nevertheless, upheld the right of a non-assenting bondholder to recover the interest from the obligor. The Court ruled that the common law right to recover interest upon the bond is of too high a character to be taken away by implications. The Court stated (p. 839):

"The mortgage was given for the purpose of securing the payment of the bonds. It contains various provisions looking to the protection of the property of the company which it covers from undue sacrifice.

It contains no provision which positively, and none, I think, which impliedly, takes away from a holder of coupons, who has taken no part in instructing the trustee as provided by the terms of the mortgage, his right of action upon them at common law."

The decision of the Circuit Court in the instant cases is in direct conflict with the decision of the Circuit Court for the Eastern District of Virginia upon the governing principles of construction of mortgage provisions with respect to the right of the majority bondholders to control the minority.

POINT II.

The decision of the Circuit Court herein holding that minority bondholders are bound by whatever action is taken by the majority when only limited authority is granted to the majority by the mortgage, is in conflict with the weight of authority.

In *Farmers Loan & Trust Co. v. Chicago & A. Ry. Co.*, 27 Fed. 146, at p. 153, the same Circuit Court which rendered the decision herein, stated:

"The right which is asserted by the majority must be found in plain and explicit terms in the mortgage or it will not be recognized. It cannot exist by mere implication."

The rule thus tersely stated by the Circuit Court for the Seventh Circuit represents the overwhelming weight of authority governing the construction of mortgage provisions pertaining to the right of majority bondholders to bind the minority.

Thus, in *Mayo v. Fitchburg & L. St. R. Co.*, 269 Mass. 118, 168 N. E. 405, the Court held that provisions in a mortgage authorizing the majority bondholders to waive a default did not include the right of the majority bondholders to bar a non-assenting bondholder from recovering on his bond. The Court pointed out that there was "nothing in the bond which makes the right of the holder contingent on the action of the majority of holders of other bonds of the series, and nothing in the trust agreement which deals with the rights of individual holders, except as against the security" (p. 121).

In *McClelland v. Norfolk S. R. Co.*, 110 N. Y. 469, the New York Court of Appeals held that mortgage provisions authorizing the majority bondholders to extend the time of payment upon a default, did not include the right of the majority bondholders to take such action in anticipation of the default.

In *Toler v. East Tenn. V. & G. R. Co.* (Cir. Ct. E. D. Tenn.), 67 Fed. 168, the Court held that mortgage provisions authorizing majority control over the right of the trustee to sell the mortgaged property would not be extended by implication to permit the majority bondholders to control the action of the trustee in foreclosure proceedings.

See also:

Meissner v. Odgen L. & I. R. Co., 65 Utah 1;

Manning v. Norfolk & Southern R. R. Co., 29 Fed. 838;

Poage v. Cooperative Publishing Co., 57 Idaho 561, 66 P. (2d) 1119;

Bulova v. Thermoid Co., 114 N. J. Law 205, 176 A. 596.

We know of no reported decision which has extended by implication the limited rights of control granted to majority bondholders under a mortgage to include "whatever action might be taken to secure payment of the bonds and coupons", as the Circuit Court herein has done. Nor do the cases cited by the Circuit Court of Appeals in its opinion tend to support the Circuit Court's ruling in this respect.

In *Sage v. Central Co.*, 99 U. S. 334, this Court upheld the right of the majority bondholders to control the disposition of the mortgage security pursuant to an express provision therefor in the mortgage. Similarly, in *Eluel, Trustee v. Fosdick*, 134 U. S. 500, this Court upheld the right of the majority bondholders, pursuant to the mortgage provision, to control the action of the trustee with respect to a foreclosure action.

We do not contend that mortgage provisions which expressly, or by necessary implication, confer upon the majority bondholders the power of control over the minority, are to be disregarded. We do contend, however, that there is no basis, in law or in equity, for the grant, through broad construction and implication, of absolute power to the majority bondholders to control the minority in "whatever action might be taken to secure the payment of the bonds and coupons".

POINT III.

The non-assenting bondholders have been deprived of their property without due process of law since the plan does not expressly or impliedly provide that their rights against the obligor shall be destroyed by the consummation of the plant, and even if it did, no reasonable opportunity was afforded to non-assenting bondholders to protect their rights by preventing the consummation of the plan.

The plan submitted by the Gas Company to its bondholders does not by any reasonable construction provide that non-assenting bondholders will be bound thereby. There is no express statement in the plan (or in the communications which accompanied the plan) to such effect and the provisions of the plan refute any such construction.

The plan is designated as an offer. It was proposed by the obligor and the bondholders took no part in the preparation or submission of the plan. The purpose of the plan is expressly stated to be for the settlement of controversies with the City (R. 291).

The plan provides for the sale, without warranty as to the mortgage, of the Gas Company properties. It does not provide for the release of the bondholders' rights in the mortgage security. The Gas Company admitted that the mortgage security still continues for all bondholders who have not accepted the plan (R. 19).

The consummation of the plan was not made dependent upon the action of a majority of the bondholders. It provided that the plan would be consummated when accepted by holders of such portion of the bonds, as the City decided would render the plan practicable (R. 293).

In the light of these provisions of the plan and in the

absence of any express statement or necessary implication to the contrary in the plan, or in the communications with respect to the plan, it is inconceivable to us, that the plan could be construed other than as an offer binding only upon those who accepted it. There is no justification for the conclusion that it bound all non-assenting bondholders.

Even if the plan could be construed as binding upon all bondholders, the actions of the Gas Company in connection with the plan should preclude it from any claim that its obligations to its bondholders have been destroyed by the consummation of the plan. The Gas Company's refusal to inform the bondholders that the consummation of the plan would bind non-assenters prevented them from taking any steps to defeat the plan. They were deprived of the opportunity to communicate with their fellow bondholders. They were misled into inaction when they could have instituted a judicial reorganization of the Gas Company, which would have guaranteed to them payment in full before the distribution of \$39 a share to stockholders. They could have compelled the Trustee to institute foreclosure proceedings.

Under all of these facts, the holding by the Circuit Court herein which did not pass upon the questions thus presented, constitutes a deprivation of petitioners' rights without due process, and should be reviewed by this Court.

Conclusion.

We respectfully submit that the ruling made by the Circuit Court in the instant cases urgently requires review by this Court in view of the numerous questions involved which vitally affect the public interest. The broad, unprecedented construction by the Circuit Court of the rights of majority bondholders, as provided in the

mortgage, threatens not only the negotiability of numerous bonds sold in the open market, but also paves the way for a general recourse by obligors to voluntary plans of reorganization with their consequent lack of judicial supervision for protection of minorities. Numerous obligors will thus be able to enrich their stockholders at the expense of their bondholders, as the Gas Company herein has accomplished under the provisions of a plan which reduced the obligations on the bonds in order to pay stockholders the substantial sum of \$39 per share.

The method adopted by the Gas Company herein also presents a threat to the rights of minorities in the precedent that it establishes for the destruction of bondholders' rights through prevention of any reasonable opportunity to the bondholders to protect such rights.

We respectfully submit that the ruling of the Circuit Court herein, and the detrimental effect to the public interest which must inevitably follow from such a ruling, warrants a review by this Court.

We respectfully submit, therefore, that the instant petition for a writ of certiorari should be granted.

Respectfully submitted,

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